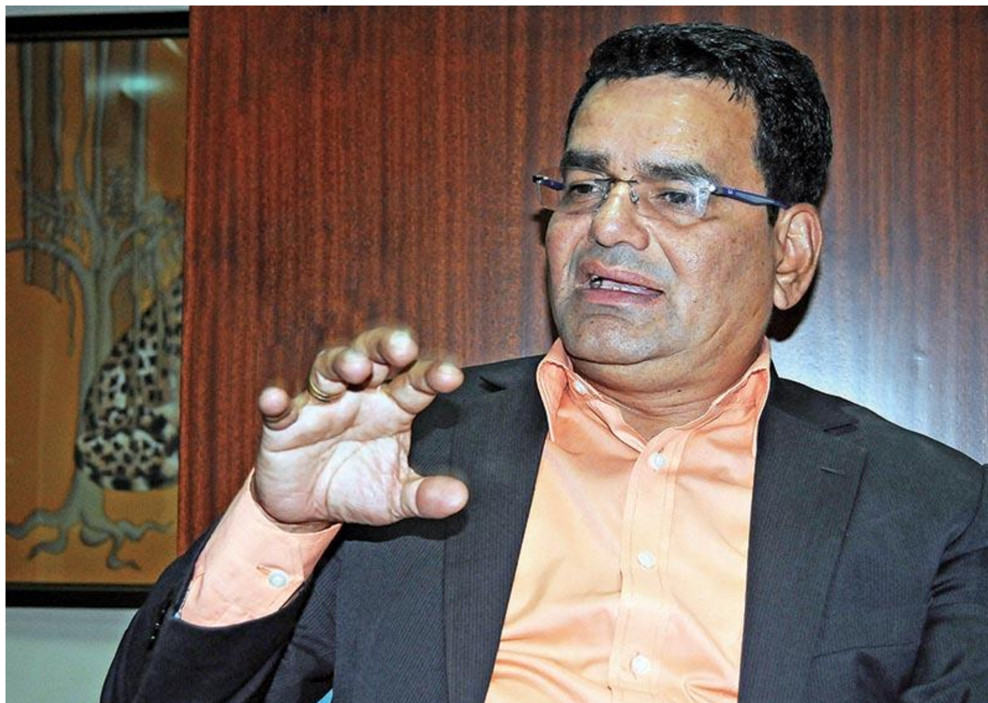
‘Unpredictability in interest rate hampering the business climate’



While coming to the end of second quarter of this fiscal, banks and financial institutions are under pressure to maintain credit to core capital plus deposit ratio at permissible level of 80 per cent. Mismatch in credit expansion and deposit collection in this fiscal has pushed BFIs on verge of overshooting CCD level. BFIs were on a very thin cushion and credit expansion was around 79 per cent of CCD by the end of five months of the fiscal. There is estimation that Rs 80 billion was withdrawn from BFIs for tax purposes since beginning of January. Pushpa Raj Acharya of *The Himalayan Times* caught up with Gyanendra Prasad Dhungana, president of Nepal Bankers’ Association and CEO of Nepal Bangladesh Bank, to learn how banks are managing the situation.

Banks are under pressure to maintain credit to core capital plus deposit ratio at permissible 80 per cent. What is your observation on withdrawal of funds and deposit collection till the end of second quarter of this fiscal?

It will be too early to comment on this as we will be receiving data of fund withdrawal and deposit collection till second quarter by Tuesday. But we have assumed that banks will not cross the allowed credit to core capital plus deposit (CCD) level. As per our estimation, around Rs 80 billion has been withdrawn since the beginning of January and banks are on a very thin cushion of around Rs 40 to Rs 45 billion to meet the permissible CCD level. They have halted loan expansion since last month as deposit growth has slowed down. Banks extended loans of around Rs 156 billion in first five months where as deposit collection was just Rs 88 billion. However, at the end of second quarter banks calculate and deposit the interest in their depositors’ accounts. Interest payment at the second quarter-end on deposit accounts will expand the deposit size to around Rs 2,184 billion from Rs 2,100 billion. On the other hand, banks are making an effort to recover matured loans and interests. Thus, I do not think the banks will breach the regulatory provisions in CCD despite withdrawal of huge fund from the banking channel for tax purposes.

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You have mentioned about the mismatch between deposit collection and credit expansion. Why did banks expand credit in such an aggressive manner?

Banks have expanded credit more patiently in this fiscal due to slow deposit growth. Deposits in the banks continue to be withdrawn for purpose of filing taxes. Meanwhile, the government has not been able to accelerate development works and post-earthquake reconstruction. We expanded credit on assumption that there will be flow of funds during elections, government's capital expenditure will gather pace and foreign direct investment will also rise as the country has moved towards stability after promulgation of the constitution and successful elections. However, they have not materialised as expected. Government's capital expenditure is low, remittance growth is negative, export is not encouraging, and foreign direct investment and capital transfer are negligible. In this scenario, it is difficult for banks to collect deposits. I have mentioned 'mismatch' because we make loan commitments as per the assumption made for deposit collection. Banks are disbursing only very critical loans since the last month as deposit growth remains sluggish. There is no blame game between Nepal Rastra Bank (NRB) and banks as the central bank always warns us regarding possible future risks and we abide by the central bank's instructions.

Banks have halted loan disbursement and are struggling to maintain CCD level. Will banks be able to book more profit in this fiscal compared to the last fiscal?

The situation is not encouraging. We have seen that average profit growth of commercial banks is below four per cent in first quarter. Many banks recorded negative profit growth and others could not expand profit substantially as their cost of deposit rose significantly. Banks have raised interest rate on deposit schemes to attract more deposits. We can expect the second quarter to be relatively better than the first quarter. For the second half it depends on how long the crisis of loanable fund prolongs. If the government accelerates development works and brings an ideal amount of funds into circulation then banks will be able to expand credit. If not they will not be able to disburse loans.

It looks like banks will have to work with low profit as their cost of deposit is high. For how long do you think will this situation prevail?

I think banks will not be able to generate double-digit profit growth for next few years as profit booked in previous years was on low paid-up capital base and it has been increased by three-folds since last fiscal. But it is not impossible. The government needs to speed up capital expenditure to achieve desired economic growth. As per studies, government needs to spend at least 10 to 13 per cent of GDP on infrastructure sector every year to bridge yawning infrastructure deficit and unleash economic potential of country. Currently, investment in infrastructure is low at around eight to nine per cent of GDP. On the other hand, government needs to promote FDI, industrialisation and boost exports, which will consequently boost capacity of banks to expand loans.

Banks say they are in a crisis of loanable funds but NRB is saying that it is not a crisis. Is it that NRB has not understood the problem being faced by banks?

The NRB is aware of this problem. We have also approached it to end the perennial problem of credit crunch especially in the third quarter of the fiscal. NRB had also discussed with Ministry of Finance on how

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an ideal amount from government treasury could be brought into circulation. We also requested government to open accounts of public enterprises in banks, so the current challenge could be addressed. However, study panel formed by MoF has said due to legal constraints funds from government treasury cannot be brought into circulation through other ways without government expenditure. Another option is refinancing facility but NRB does not have adequate funds to provide refinancing facility. NRB has fund of around Rs 20 billion to provide refinancing facility whereas according to NRB rules banks can obtain refinancing facility of up to 25 per cent of core capital. This means banks can mobilise around Rs 70 billion but NRB has only a small amount available. There has been misinterpretation about liquidity and loanable fund crisis. Banks can extend loans of up to 80 per cent of core capital plus deposits and of remaining 20 per cent six per cent is with NRB as cash reserve, around five per cent remains as liquid cash in bank vaults, and eight to nine per cent is invested in government bonds/treasury products. Liquidity crisis is when there is pressure on cash reserve in NRB. We are in a comfortable liquidity position as there is around Rs 50 billion liquidity in banking system. Crisis is only regarding loanable fund as almost all banks are close to permissible CCD level of 80 per cent.

NRB Governor Chiranjibi Nepal recently said that banks are more urban centric and have not made efforts to attract deposits. What do you have to say on this?

That is partially true as there is a high percentage of unbanked population and there is space to expand outreach. As per NRB’s instruction we are expanding branch network in 130 rural municipalities and this will help us to collect deposits. Banks have also expanded their services through mobile banking. Banks are doing their best to collect deposits as they are facing scarcity of fresh deposits and interest rate is fluctuating frequently. Unpredictability in interest rate is also hampering business climate. This is why NRB needs to look into policies that could be obstructing flow of deposits to the banks.

Source: The Himalayan Times, 15th January 2018